

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

**FINANCIAL STATEMENTS WITH
INDEPENDENT AUDITORS' REPORT**

For the Years Ended December 31, 2010, and 2009

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Ottawa County, Kansas
Rural Water District No. 2
Salina, Kansas 67402

We have audited the financial statements of Ottawa County Rural Water District No. 2, as of and for the years ended December 31, 2010 and 2009, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the *Kansas Municipal Audit Guide*. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position of Ottawa County Rural Water District No. 2, as of December 31, 2010 and 2009 and the results of operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 2-3 and the budget report on page 13 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted by the United States of America. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However we did not audit the information and express no opinion on it.

Pottberg, Gassman & Hoffman, Chtd.

POTTBERG, GASSMAN & HOFFMAN, CHARTERED

Manhattan, Kansas
June 27, 2011

MEMBERS:
American Institute of
Certified Public Accountants

Kansas Society of Certified
Public Accountants



OTTAWA COUNTY RURAL WATER DISTRICT NO. 2

MANAGEMENT'S DISCUSSION AND ANALYSIS

Within this section of the Ottawa County Rural Water District No. 2's annual financial report, the District's management provides narrative discussion and analysis of the financial activities of the District for the year ended December 31, 2010. The District's financial performance is discussed and analyzed within the context of the accompanying financial statements and disclosures following this section.

In 2010, the district added four (4) units, making a total of 858 units. In 2010 the annual usage was 64,386,000 gallons of water, which showed an annual loss of 5.32%. Since we are a customer read district, the Board of directors has implemented a policy that a staff member will read all the meters once a year and whenever necessary to help maintain a reasonable yearly percentage loss. The district continually communicates with customers to keep the accounts receivable to a minimum.

After preparing the annual budget for 2010, the water district believed they were in compliance with the bond covenants and the rates for water and minimum charge were sufficient. The Business Manager prepared the 2011 annual budget, as required by the BYLAWS of the District (see Article 8, Powers and Duties of Directors. Paragraph G). The water district then realized they were not in compliance with the bond covenants as the rates for water and minimum charge were insufficient to maintain the required debt service ratio. As a result, in April 2011 the District approved increased water and minimum usage rates effective July 1, 2011 and revised the 2011 annual budget. With the assistance of Ransom Financial it is estimated that the rate increase will result in additional water revenue of \$58,000 during 2011.

In pursuing the new sources of water for the water district, an "Agreement for Temporary Easement and Option to Purchase" was obtained from Mildred Moorman Revocable Trust. The water district hired Ned Marks with Terrane Resources as the Hydrogeologist. After test holes and test wells were drilled there were large amounts of good sand formation found on the property. The presence of good quality water and good volume of water are very promising. Additional drilling and testing will follow.

A developer approached the Board to develop 35 lots on the quarter section immediately North of the well field of the District. The process to drill monitoring wells on the property is on going for protection of the District well field.

The new 200,000 gallon water tower on Country Club Road was constructed and placed in use by the end of the year.

The district sought bids for an additional well on Ohio Street to be placed in a battery of wells with well No. 3. Pestinger Pump Service was the only bidder with a bid of \$71,995.00. The well was completed and put into service with the other wells.

The Board accepted the estimate of \$12,997.30 from the Kansas Rural Water Association for GPS mapping Assistance Program. A grant from the Kansas Water Office would fund half or not to exceed \$4,000.00. The GPS mapping is being completed by Kansas Rural Water Association.

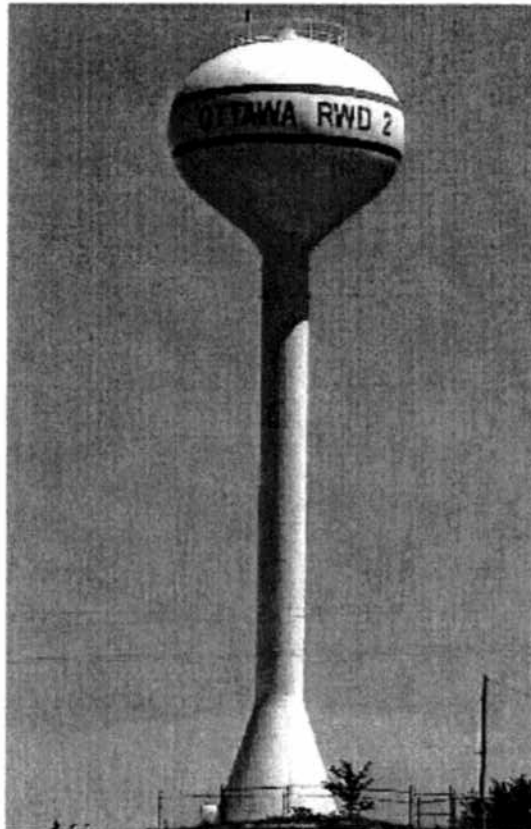
All the substantial interest statements were completed and returned to the district.

The water district has an emergency disaster plan and a conservation plan in effect.

Since there are four employees and one contract worker of the district that are related, all their invoices and requests for reimbursement statements will be reviewed and signed by one of the Board members. Also, in the event a monthly meeting is not held, the bank account check

register of the district will be presented to the Board of Directors for approval. This will show all invoices and payroll that was paid and all monies deposited. Each month the reconciliation of the bank accounts and bank statements will be reviewed and signed by the Chairman of the District. The checks have two signatures as required.

Should you have any questions concerning this report or any other water district matter, feel free to call 785.823.2093.



New water tower, Ottawa County Rural Water District No. 2

OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
STATEMENTS OF NET ASSETS
DECEMBER 31,

ASSETS	<u>2010</u>	<u>2009</u>
Current Assets		
Cash in Bank	\$ 645,977	\$ 861,992
Accounts Receivable - Net	6,721	5,315
Inventory	17,846	22,081
Prepaid Expenses	-	833
Total Current Assets	<u>670,544</u>	<u>890,221</u>
Noncurrent Assets		
Construction Work in Progress	94,585	-
Capital Assets		
Engineering Costs	149,396	132,970
Office Equipment	25,247	25,247
Property Easements	9,380	9,368
Property Easements well 5 6 7	43,920	43,920
Standpipe Easements	4,500	4,500
Water Transmission and Distribution System	4,141,983	3,581,298
Water Wells and Easements	110,635	36,369
New Well Project	28,587	28,587
Accumulated Depreciation	<u>(1,855,477)</u>	<u>(1,751,953)</u>
Total Capital Assets	2,752,756	2,110,306
Bond Issuance & Discount Costs - 2001 (net of accumulated amortization of \$32,888 and \$29,267)	3,319	6,940
Bond Issuance Costs - 2004 (net of accumulated amortization of \$5,672 and \$4,764)	12,478	13,386
Bond Issuance Costs - 2009 (net of accumulated amortization of \$905 and \$69)	15,807	16,643
2004 Bond Proceeds	490,116	487,328
Certificates of Deposit - 2001 Bond Reserve	261,415	254,547
Certificate of Deposit - 2004 Bond Reserve	97,530	94,518
Certificate of Deposit - 2009 Bond Reserve	80,545	78,563
2009 Bond Proceeds	<u>322,866</u>	<u>775,052</u>
Total Noncurrent Assets	<u>4,036,832</u>	<u>3,837,283</u>
TOTAL ASSETS	<u>\$4,707,376</u>	<u>\$4,727,504</u>
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts Payable	\$ 72,203	\$ 255
Accrued Interest Payable	20,017	12,887
Payroll Liabilities	1,719	1,213
Deferred Revenue	69,567	63,682
Bonds Payable - Current Portion	<u>215,000</u>	<u>165,000</u>
Total Current Liabilities	<u>378,506</u>	<u>243,037</u>
Noncurrent Liabilities		
Bonds Payable - 2001 Bond Issue (less current portion of \$215,000 and \$165,000)	-	215,000
Bonds Payable - 2004 Bond Issue	780,000	780,000
Discount on 2004 Bonds (net of accumulated amortization of \$4,631 and \$3,890)	(10,189)	(10,930)
Bonds Payable - 2009 Bond Issue	885,000	885,000
Discount on 2009 Bond (net of accumulated amortization of \$839 and \$64)	<u>(14,648)</u>	<u>(15,423)</u>
Total Noncurrent Liabilities	<u>1,640,163</u>	<u>1,853,647</u>
Total Liabilities	<u>2,018,669</u>	<u>2,096,684</u>
Net Assets		
Invested in Capital Assets, net of related debt	897,593	91,659
Restricted 2001 Bond Reserve	148,500	148,500
Restricted 2004 Bond Reserve	78,000	78,000
Restricted 2009 Bond Reserve	78,563	78,563
Unrestricted	<u>1,486,051</u>	<u>2,234,098</u>
Total Net Assets	<u>2,688,707</u>	<u>2,630,820</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$4,707,376</u>	<u>\$4,727,504</u>

The notes to the financial statements are an integral part of this statement.

OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31,

	<u>2010</u>	<u>2009</u>
OPERATING REVENUES		
Water Sales	\$ 458,749	\$ 445,444
OPERATING EXPENSES		
Accounting Fees	5,890	5,620
Attorney Fees	1,815	3,132
Chlorine Fees	6,945	5,555
Clean Drinking Water Fees	1,744	1,680
Contract Wages	63,512	51,753
Dues and Subscriptions	653	675
Easements	-	48
Fees and Permits	25	-
Insurance	11,725	9,787
Internet Fee	624	560
IRA Contributions	2,065	1,748
Lab Fees	3,445	524
Mileage	18,455	16,870
Miscellaneous	2,568	2,334
Office Supplies Expense	5,953	4,574
Payroll Taxes	5,911	4,810
Power	24,666	23,786
Professional Fees	-	2,230
Repairs and Maintenance	11,338	17,577
Salaries and Wages	77,269	62,878
Supplies Expense	6,930	3,995
Telephone	7,009	6,863
Water Protection Fees	1,861	1,792
TOTAL OPERATING EXPENSES	<u>260,403</u>	<u>228,791</u>
INCOME FROM OPERATIONS BEFORE		
AMORTIZATION AND DEPRECIATION	198,346	216,653
Amortization	(6,879)	(5,403)
Depreciation	<u>(103,525)</u>	<u>(100,268)</u>
OPERATING INCOME (LOSS)	<u>87,942</u>	<u>110,982</u>
NON-OPERATING REVENUES AND EXPENSES		
Interest Income	35,012	39,213
Other Income	5,600	14,643
Interest Expense	<u>(90,667)</u>	<u>(53,136)</u>
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>50,055</u>	<u>720</u>
INCOME (LOSS) BEFORE CONTRIBUTIONS	37,887	111,702
Capital Contributions	<u>20,000</u>	<u>28,200</u>
CHANGE IN NET ASSETS	57,887	139,902
NET ASSETS, BEGINNING	<u>2,630,820</u>	<u>2,490,918</u>
NET ASSETS, ENDING	<u><u>\$ 2,688,707</u></u>	<u><u>\$ 2,630,820</u></u>

The notes to the financial statements are an integral part of this statement.

OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,

	<u>2010</u>	<u>2009</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash Received from Customers	\$ 463,228	\$ 443,962
Cash Payments to Suppliers for Goods and Services	(99,706)	(99,715)
Cash Payments to Employees and Professional Contractors for Services	(151,248)	(132,585)
Net Cash Provided (Used) by Operating Activities	<u>212,274</u>	<u>211,662</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition and Construction of Capital Assets	(677,900)	(143,243)
Principal Paid on Bonds	(165,000)	(155,000)
Interest Paid on Bonds	(83,537)	(54,725)
Proceeds from Bond Issue	449,398	107,518
Issuance and Discount on Bonds	-	(32,200)
Bond Reserve Decrease (Increase)	(11,862)	(105,529)
Other Capital Activities	5,600	14,643
Capital Contributions	20,000	28,200
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(463,301)</u>	<u>(340,336)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment Income	<u>35,012</u>	<u>70,635</u>
Net Cash Provided (Used) by Investing Activities	<u>35,012</u>	<u>70,635</u>
 Net Increase (Decrease) in Cash and Cash Equivalents	 (216,015)	 (58,039)
Cash and Cash Equivalents at January 1	861,992	920,031
Cash and Cash Equivalents at December 31	<u>\$ 645,977</u>	<u>\$ 861,992</u>
 Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Income from Operations	\$ 198,346	\$ 216,653
Changes in Receivables	(573)	(609)
Changes in Inventory	4,235	(3,095)
Changes in Payables less Capitalized Expense	4,381	419
Changes in Deferred Revenue	5,885	(1,706)
Net Cash Provided by Operating Activities	<u>\$ 212,274</u>	<u>\$ 211,662</u>

The notes to the financial statements are an integral part of this statement.

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 - ORGANIZATION DESCRIPTION AND ACCOUNTING POLICIES

The Rural Water District No. 2, Ottawa County, Kansas (District), was declared incorporated as a municipal Corporation by the Board of Commissioners of Ottawa County, Kansas. The board of directors for the district adopted bylaws at a meeting of the landowners of the district on June 11, 1979.

Measurement Focus, Basis of Accounting, and Financial State Presentation

The water district is a governmental organization operated as a business (proprietary) type entity. Its is accounted for using the "economic resources" measurement focus and the accrual basis of accounting, in conformity with accounting principles generally accepted in the United States of America. All assets and liabilities are included on the Statements of Net Assets. The Statements of Revenues, Expenses and Changes in Net Assets presents increases (revenues) and decreases (expenses) in total assets, and revenues are recognized in the period in which they are earned while expense are recognized in the period in which the liability is incurred.

Operating revenues are those that are generated from primary operations. All other revenues are reported as non-operating revenues. Operating expenses are those expenses that are essential to the primary operations. All other expenses are reported as non-operating expenses, such as installation fees and reimbursement for benefit units.

Statements of Cash Flows

For purposes of the statement of cash flows, the District considers all highly liquid investments including bank deposit accounts, money market accounts and certificates of deposit classified as current assets to be cash and cash equivalents. Certificates of deposit with maturities of longer than three months can still be used by the district to meet current liabilities if they wish to pay any applicable penalties.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain amounts and disclosures. Accordingly, actual results could differ from those estimates.

Capital Assets

Capital assets purchased are capitalized at cost. Depreciation is recorded based on the estimated useful life of each asset using the straight-line method. The District's policy is to capitalize all assets with a cost of \$500 or more and a useful life exceeding one year.

Inventory

Inventory is stated at cost and consists of pipe, valves, meters, and other items needed to repair water lines.

NOTE 2 – DEPOSITS AND INVESTMENTS

K.S.A. 9-1401 establishes the depositories which may be used by the District. The statute requires banks eligible to hold the District's funds have a main or branch bank in the county in which the District is located, or in an adjoining county if such institution has been designated as an official depository, and the banks provide an acceptable rate of return on funds. In addition, K.S.A. 9-1402 requires the banks to pledge securities for deposits in excess of FDIC coverage. The District has no other policies that would further limit interest rate risk.

K.S.A. 12-1675 limits the District's investment of idle funds to time deposits, open accounts, and certificates of deposit with allowable financial institutions; U.S. government securities; temporary

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

NOTES TO THE FINANCIAL STATEMENTS

NOTE 2 – DEPOSITS AND INVESTMENTS (CONTINUED)

notes; no-fund warrants; repurchase agreements; and the Kansas Municipal Investment Pool. The District has no investment policy that would further limit its investment choices.

Concentration of credit risk. State statutes place no limit on the amount the District may invest in any one issuer as long as the investments are adequately secured under K.S.A. 9-1402 and 9-1405.

Custodial credit risk – deposits. Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. State statutes require the District's deposits in financial institutions to be entirely covered by federal depository insurance or by collateral held under a joint custody receipt issued by a bank within the State of Kansas, the Federal Reserve Bank of Kansas City, or the Federal Home Loan Bank of Topeka, except during designated "peak periods" when required coverage is 50%. The District has no designated "peak periods." All deposits were legally secured at December 31, 2010 and 2009.

At December 31, 2010 the District's carrying amount of deposits was \$1,898,449 and the bank balance was \$1,900,688. The bank balance was held by 5 banks with four holding more than 5% of the total bank balance, resulting in a concentration of credit risk. Of the bank balance, \$927,892 was covered by federal depository insurance and \$409,814 was collateralized with securities held by the pledging financial institutions' agents in the District's name and \$562,982 was collateralized with securities held by the pledging financial institutions' agents in a third party name.

The following is a comparison of depository security with balances on deposit with the District's designated depositories:

	Demand Deposits on <u>12/31/2010</u>	Time Deposits on <u>12/31/2010</u>	FDIC Coverage	Pledged Securities	Unsecured Deposits
Bennington State Bank	\$92,467	\$348,133	\$250,000	\$190,600	-
Bank of Tescott	-	469,214	250,000	219,214	-
Great Plains FCU	1,838	78,524	80,362	-	-
United Bank & Trust	812,982	-	250,000	562,982	-
First Bank Kansas	-	97,530	97,530	-	-

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable are customer water bills that have been invoiced but remain unpaid. The balance is shown net of the allowance for doubtful accounts. Using past payment history and the aging report, the allowance as of December 31, 2010 and 2009 has been determined to be zero.

NOTE 4 – CAPITAL ASSETS

During 2004 the District's infrastructure assets were estimated using expenditures of prior years and are stated retrospectively. The water distribution system, wells and related easements and engineering costs are being depreciated over 40 years.

Balance <u>01-01-10</u>	Accumulated Depreciation	Purchases	Disposals	Depreciation	Balance <u>12-31-10</u>
<u>\$3,862,259</u>	<u>(\$1,751,952)</u>	<u>\$651,389</u>	<u>(\$ 0)</u>	<u>(\$103,525)</u>	<u>\$2,658,171</u>

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

NOTES TO THE FINANCIAL STATEMENTS

NOTE 5 – DEFERRED REVENUE

Multiple District customers have paid in advance for water usage. These amounts have not been earned and would be refundable if water usage discontinues. The balance of these customer credits was \$69,567 at December 31, 2010 and \$63,682 at December 31, 2009.

NOTE 6 – BONDS PAYABLE

On December 1, 2001, the district issued \$1,485,000 in Kansas Rural Water Finance Authority Revenue Bonds, Series B, 2001 with effective interest rates ranging from 2.50% to 4.75% to refund their Kansas Rural Water Finance Authority Revenue bonds, Series C, 1996 in the amount of \$1,455,000. Interest payments are due semi-annually on October 1 and April 1. Principal payments are due on April 1 maturing in 2011.

On August 1, 2004, the district issued \$780,000 in Kansas Rural Water Finance Authority Revenue Bonds, Series C, 2004 with effective interest rates ranging from 3.85% to 5.00%. The purpose of the bond issue was to construct a second main under I-70 (completed in 2005), develop a new well (completed in 2007) and construct a new chlorination building as well as remodel the existing chlorination building. Work has not yet begun on the chlorination buildings. Interest payments are due semi-annually on April 1 and October 1. Principal payments are due starting on October 1, 2012 and maturing in 2024.

On December 1, 2009, the district issued \$885,000 in Kansas Rural Water Finance Authority Revenue Bonds, Series B, 2009 with effective interest rates ranging from 1.75% to 4.75%. The purpose of the bond issue is to purchase a water tower. Interest payments are due semi-annually on June 1 and December 1. Principal payments are due starting on December 1, 2010 and maturing in 2029.

2001 Bonds Payable Information:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Payment</u>
2011	<u>215,000</u>	<u>4,569</u>	<u>219,569</u>
Totals	<u>\$215,000</u>	<u>\$4,569</u>	<u>\$219,569</u>

Issuance costs of \$23,912 were paid at the time this revenue bond was issued in 2001. This cost was capitalized and is being amortized over the life of the revenue bonds using the straight-line method. Amortization for 2010 and 2009 was \$2,391 each year. The bonds were issued at a discount of \$12,295 which is amortized over the life of the bonds using the straight-line method. Amortization for 2010 and 2009 was \$1,230 each year. A bond reserve account of \$148,500 is required to be maintained. Four certificates of deposit, one at Bennington State Bank in the amount of \$37,425 and three at Bank of Tescott in the amounts of \$43,028, \$153,374 and \$27,588 totaling \$261,415 are designated as bond reserve.

2004 Bonds Payable Information:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Payment</u>
2011	-	35,480	35,480
2012	\$50,000	35,480	85,480
2013	50,000	33,555	83,555
2014	50,000	31,555	81,555
2015	50,000	29,505	79,505
2016-2020	285,000	113,455	398,455
2021-2024	<u>295,000</u>	<u>37,720</u>	<u>332,720</u>
Totals	<u>\$780,000</u>	<u>\$316,750</u>	<u>\$1,096,750</u>

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

NOTES TO THE FINANCIAL STATEMENTS

NOTE 6 – BONDS PAYABLE (CONTINUED)

Issuance costs of \$18,150 were paid at the time this revenue bond was issued. The cost was capitalized and is being amortized over the life of the revenue bonds, using the straight-line method. Amortization for 2010 and 2009 was \$907 each year. The bonds were issued at a discount of \$14,820 which is amortized over the life of the bonds using the straight-line method. Amortization for 2010 and 2010 was \$741 each year. A bond reserve account of \$78,000 is required to be maintained. \$97,530 is segregated as a Certificate of Deposit at First Bank Kansas.

2009 Bonds Payable Information:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total Payment</u>
2011	-	35,450	35,450
2012	\$30,000	35,450	65,450
2013	35,000	34,850	69,850
2014	35,000	34,045	69,045
2015	35,000	33,135	68,135
2016-2020	210,000	145,865	355,865
2021-2025	270,000	99,185	369,185
2026-2029	<u>270,000</u>	<u>33,040</u>	<u>303,040</u>
Totals	<u>\$885,000</u>	<u>\$451,020</u>	<u>\$1,336,020</u>

Issuance costs of \$16,712 were paid at the time this revenue bond was issued. The cost was capitalized and is being amortized over the life of the revenue bonds, using the straight-line method. Amortization for 2010 was \$836 and for 2009 was \$69. The bonds were issued at a discount of \$15,487 which is amortized over the life of the bonds using the straight-line method. Amortization for 2010 was \$775 and for 2009 was \$64. A bond reserve account of \$78,563 is required to be maintained. \$80,545 is segregated as a Certificate of Deposit at Bennington State Bank.

NOTE 7 – DEBT SERVICE RATIO

The bond issue covenants require the District to maintain a debt service ratio of at least 1.25.

**Debt Service Ratio Calculation for the
year ending:**

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
Change in Net Assets	\$57,887	\$139,902
Interest Expense	90,667	53,136
Amortization & Depreciation	110,404	105,671
Less Capital Contributions	<u>(20,000)</u>	<u>(28,200)</u>
Total Revenue Available for Debt Service	<u>\$238,958</u>	<u>\$270,509</u>
Debt Service Payments	\$248,537	\$209,725
Debt Service Ratio	<u>1.04</u>	<u>1.29</u>

As described in NOTES 15 and 16, the District is in violation of their bond covenants. Steps have been taken to increase the debt service ratio in 2011.

**OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS**

NOTES TO THE FINANCIAL STATEMENTS

NOTE 8 – LONG TERM DEBT SCHEDULE

The following schedule shows the changes in long-term debt and related maturities.

<u>Revenue Bonds</u>	<u>Date Issued</u>	<u>Original Amount</u>	<u>Outstanding 01-01-09</u>	<u>Principal Payments</u>	<u>Outstanding 12-31-09</u>	<u>Interest Paid In 2010</u>
2001	12-01-01	\$1,485,000	\$380,000	\$165,000	\$215,000	\$12,602
2004	08-01-04	780,000	780,000	-	780,000	35,485
2009	12-01-09	<u>\$885,000</u>	<u>885,000</u>	<u>-</u>	<u>\$885,000</u>	<u>35,450</u>
Total Indebtedness		<u>\$3,150,000</u>	<u>\$2,045,000</u>	<u>\$165,000</u>	<u>\$1,880,000</u>	<u>\$83,537</u>

NOTE 9 – BUDGETS AND BUDGETARY ACCOUNTING

The District is not required to adopt a legal budget; therefore, no budgetary comparison is prepared as a financial statement. The Board approves a budget each year, which is used by management to internally monitor the District's expenditures and is presented as supplementary information.

NOTE 10 - RETIREMENT PLAN

The district provides a Simple IRA for the full time employees as retirement compensation. The District contributes 3% of the employees' wages to these IRAs. In 2010, the District contributed \$2,065 and in 2009, \$1,748 to the retirement plan. The IRAs are with American Funds.

NOTE 11 - COMPENSATED ABSENCES POLICY

The District provides vacation leave for the Business Manager. There is no written policy for the carry forward of unused time nor for the payment of unused time at termination or retirement. Therefore no accrual has been made.

NOTE 12 - LITIGATION

There were no legal actions involving the District as of December 31, 2010.

NOTE 13 – RELATED PARTIES

All the members of the board of directors are water district customers. The only material transactions were water purchases consummated on the same terms as all other water customers.

NOTE 14 – RISK MANAGEMENT

Ottawa County Rural Water District No. 2 is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To insure against risk of these types of losses, the District has purchased commercial insurance coverage from EMC Companies through Anderson Peck Agency Inc. in Topeka, Kansas. Settled claims resulting from these risks have not exceeded commercial coverage.

NOTE 15 – CONTINGENCIES

As detailed in NOTE 7 the District is in violation of a bond covenant requiring a debt service ratio of 1.25. In the process of adding new wells financed by the bonds the District has used many man hours of the their own staff. Their recordkeeping did not provide the ability to capitalize the

OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
SALINA, KANSAS

NOTES TO THE FINANCIAL STATEMENTS

NOTE 15 – CONTINGENCIES, (CONTINUED)

corresponding wage and benefit costs. As a result the debt service ratio decreased due these costs that were not capitalized. The District had sufficient cash available to make the debt service payments. As disclosed in NOTE 16, the District has raised water rates during 2011 which should produce additional revenue to increase the debt service ratio to the required amount in future years. In addition, the District is in a position to make the 2011 debt service payments from available cash. During 2011 the 2001 Bond issue will be paid in full and subsequent years debt service payments will be significantly reduced. The District does not feel that debt service ratio violation will cause the bonds to be called or reduce their credit standing in anyway.

NOTE 16 – SUBSEQUENT EVENTS

Management has performed an analysis of the activities and transactions subsequent to December 31, 2010 to determine the need for any adjustments to and / or disclosures within the audited financial statements. Management has performed their analysis through June 27, 2011, which is the date at which the financial statements were available to be issued.

In order to assist in meeting the required debt service ratio, the District implemented a new rate schedule effective as of July 1, 2011. The new rate schedule is \$3.50 per 1,000 gallons with a minimum rate set at \$35.00per month. The previous rate schedule was \$3.00 per 1,000 gallons with a minimum rate of \$27.00 per month. With the assistance of Ransom Financial, it was estimated this rate increase would generate and additional \$58,000 of revenue during 2011.

OTTAWA COUNTY RURAL WATER DISTRICT NO. 2
BUDGET REPORT - CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2010

	<u>Budget</u>	<u>Actual</u>	Variance Over (Under)
OPERATING REVENUES			
Water Revenues	\$ 448,000	\$ 463,228	\$ 15,228
OPERATING EXPENSES			
Chlorine Fee	6,400	6,945	545
Clean Drinking Water Fee	1,710	1,744	34
Contract Wages	60,000	63,512	3,512
Dues and Subscriptions	725	653	(72)
Fees and Permits	-	25	25
Insurance	10,100	11,725	1,625
Internet Fee	-	624	624
IRA Contributions	2,000	2,065	65
Lab Fees	-	3,445	3,445
Mileage	16,000	18,455	2,455
Miscellaneous	22,650	2,568	(20,082)
Office Supplies Expense	4,500	5,953	1,453
Payroll Taxes	5,000	4,572	(428)
Power	24,000	24,666	666
Professional Fees	23,000	7,705	(15,295)
Repairs and Maintenance	7,500	3,228	(4,272)
Salaries & Wages	70,000	77,269	7,269
Supplies Expense	2,500	6,930	4,430
Telephone	5,200	7,009	1,809
Water Protection Fee	1,825	1,861	36
TOTAL OPERATING EXPENDITURES	<u>263,110</u>	<u>250,954</u>	<u>(12,156)</u>
DEBT RETIREMENT:			
Bond Principal Paid	165,000	165,000	-
Bond Interest	83,533	83,537	4
TOTAL EXPENDITURES	<u>511,643</u>	<u>499,491</u>	<u>(12,152)</u>
OTHER INCOME (EXPENSES)			
New Benefit Units	25,000	20,000	(5,000)
Interest Income	45,000	35,012	(9,988)
Other Income and Expense	100,000	443,136	343,136
Capital Improvements	(629,753)	(677,900)	48,147
TOTAL OTHER INCOME (EXPENSE)	<u>(459,753)</u>	<u>(179,752)</u>	<u>(280,001)</u>
INCREASE (DECREASE) IN CASH	<u>\$ (523,396)</u>	<u>\$ (216,015)</u>	<u>\$ 307,381</u>

The notes to the financial statements are an integral part of this statement.